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Competitive Advantage in the Business Environment: The Role of Innovation and Knowledge Management in Sago-Processing MSMEs in the Meranti Islands Regency

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A B S T R A C T

This study discusses the role of innovation and knowledge management in achieving competitive advantage for sago-processing MSMEs in the Meranti Islands Regency. The sample consisted of 95 sago-processing MSMEs located in the Meranti Islands Regency. This study argues that innovation is essential for product development and differentiation, whereas knowledge management is crucial for the creation, validation, presentation, distribution, and application of knowledge. This study also highlights the importance of dynamic capabilities in enhancing competitiveness and achieving a competitive advantage in the business environment. The study found that sago-processing MSMEs in the Meranti Islands Regency face challenges in adapting to changes in the business environment because of the absence of innovation in their products and insufficient knowledge management. The study concluded by emphasizing the need for sago-processing MSMEs to adopt innovation and knowledge management strategies to achieve a competitive advantage in the market

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INTRODUCTION

The ongoing global hurdle confronting organizations is the volatile nature of their business environments. The environment in which businesses operate is constantly changing, adapting to the progress and evolving trends of the present era. As Risdwiyanto (2017) noted, this dynamic environment is characterized by continuous evolution and shifts, and changes in the business environment ultimately lead to uncertainties that must be adapted continuously by companies. The dynamic development of business has a significant influence on the changes in the dimensions of every aspect of human life, one of which is the economic aspect that leads the business world to intense competition. To remain competitive in a highly competitive market, businesses must carefully navigate changes in the business environment by analyzing market conditions and consumer demands and desires. This approach allows companies to gain an advantage over their competitors and achieve a competitive edge.

Heizer and Render (2015) claimed that competitive advantage is achieved indirectly through the establishment of a system that possesses a significant advantage over its rivals. According to Heizer and Render (2015), achieving a competitive advantage can be accomplished through various methods such as differentiation, low-cost strategies, and responsiveness to consumer needs. Furthermore, innovation can help a company gain competitive edge. According to Sugiono and Efendi (2019), innovation exerts a favorable and statistically significant impact on enhancing competitive advantage.

In line with Schumpeter's (1934) work, as referenced by Wawan et al. (2020), innovation is defined as the process through which entrepreneurs create a unique configuration of production factors. This innovative thinking is considered a crucial driving force in stimulating economic growth. Schumpeter's (1994) theory of innovation comprises five key components: product innovation, process innovation, market innovation, utilization of novel materials, and acquisition of raw materials. Innovation is not only closely related to competitive advantage but is also closely linked to knowledge. According to Wawan et al. (2020), innovation stems from a company's ability to manage, maintain, and create knowledge. Innovation is essentially born from the knowledge possessed by a company, which is then developed into something new. Forcadell and Guadamillas (2002) stated that organizations' utilization of knowledge management strategies can lead to the development of sustainable innovation processes that involve all members of the company.

Achieving competitive advantage in the business world can be attained not only through the innovation process but also through the application of knowledge management. According to Bhatt (2001), as cited in Lee et al. (2016), knowledge management is the process of creating, validating, presenting, distributing, and applying knowledge, through which a company's strategy for achieving competitive advantage can be achieved. Laila et al. (2021) find that knowledge management has a positive effect on competitive advantage. Given rapid and dynamic changes in the business environment, companies face new challenges in continuously improving their competitiveness. In this case, dynamic capabilities become one of the factors that influence a company's ability

to enhance its competitiveness and achieve competitive advantage in the dynamics of the business environment. According to Teece et al. (1997), dynamic capability refers to an organization's ability to effectively combine, develop, and restructure its internal and external skills in response to swift shifts in environmental conditions. Michael and Widjojo (2021) find that dynamic capabilities have a positive and significant effect on competitive advantage.

Environmental change poses a significant challenge for sago-processing MSMEs in the Meranti Islands Regency, which continues to operate in a traditional manner. The MSMEs in the Meranti Islands Regency appear to be less responsive to changes in the business environment and encounter obstacles when attempting to adapt to such changes. The low level of adaptation exhibited by these MSMEs can be attributed to the absence of innovation in their products, which hinders their ability to achieve a competitive advantage in the market. The insufficient innovation of micro-, small-, and medium-sized enterprises (MSMEs) is clearly demonstrated by the unattractive design and packaging of sago-processed products in the Meranti Islands Regency, as well as the subpar quality of products marketed by some MSMEs that have yet to satisfy the standards established by the Indonesian Food and Drug Administration (BPOM) (Imron, 2020).

The Meranti Islands Regency's sago-processing micro, small, and medium enterprises (MSMEs) struggle with the capacity to create novel products in the context of product innovation. MSMEs typically concentrate on producing conventional items like sago rendang, sago lemak, or sago crackers. Sago-processing MSMEs offer limited product variations without innovation to create new products that are more attractive to the market. The sago-processing MSMEs of the Meranti Islands Regency encounter constraints during the production process. The aforementioned constraints are manifested in conventional and less productive production techniques that have not experienced substantial advancements, as demonstrated by the utilization of rudimentary equipment and machinery, as well as the prevalence of manual procedures. In the realm of market innovation, sago-processing micro, small, and medium enterprises (MSMEs) in the Meranti Islands Regency have yet to embrace marketing innovation. The inadequate understanding of business promotion through e-commerce is a significant hurdle that can impede the progress of MSMEs (Yuningsih and Silaningsih, 2020). The inefficiency of traditional marketing techniques can be seen in the absence of modern technology and strategies, particularly in methods that rely solely on word-of-mouth promotions.

LITERATURE REVIEW

Competitive Advantage

As defined by Porter (2020), competitive advantage refers to a company’s capacity to outperform its industry or market peers through its unique characteristics and resources. Porter (2020) identified three generic competitive strategies: cost advantage, differentiation, and focus. Setiawan (2012) classifies competitive advantage indicators into three categories: product uniqueness, product quality, and competitive pricing.

Knowledge Management

According to Nonaka and Takeuchi (1995) in Dalkir (2011), knowledge management refers to a systematic approach aimed at capturing, organizing, managing, and disseminating knowledge throughout an organization, with the ultimate goal of enabling employees to work more efficiently, reuse best practices, and reduce redundant expenses. Alavi and Leidner (2001) identified four stages of the knowledge management process: knowledge creation, knowledge storage, knowledge transfer, and knowledge application.

Dynamic Capabilities

According to Teece et al. (2018), dynamic capabilities encompass a company's capacity to integrate, build, and reconfigure its internal and external competencies to address rapidly changing environments. Wang and Ahmed (2007) characterized dynamic capabilities as a company's continuous behavioral orientation towards integrating, reconfiguring, renewing, and recreating resources and capabilities. Most importantly, it enhances and reconstructs its core capabilities in response to environmental changes to achieve and maintain a competitive advantage. Teece (2007) identified three dimensions of dynamic capabilities: sensing, capturing, and transforming capabilities.

Innovation

Innovation is commonly understood as the introduction of new concepts, methods, or items that are intentionally embraced by an individual, group, or organization (Rogers, 1983). Everett M. Rogers identifies five key features of innovation, including compatibility, complexity, relative advantage, visibility, and trialability. Mabenge et al. (2022) state that enterprises may employ three dimensions of innovation: product innovation, process innovation, and market innovation.

METHODOLOGY

This study employed a quantitative research design. This research was carried out among sago-processing MSMEs in the Meranti Islands Regency. The population for this study comprised 95 sago-processing MSMEs registered with the Department of Cooperatives, MSMEs, and Labor of the Meranti Islands Regency. Saturated sampling was used in this study, resulting in a sample size of 95 respondents. Questionnaires were used for data collection, and data analysis was conducted using the Structural Equation Modeling (SEM) method with the assistance of SmartPLS 3.0, starting with a descriptive statistical analysis.

The evaluation of the second-order construct using an embedded two-stage approach for the measurement model in this study (Hair et al., 2021) was conducted in two stages. The initial stage involved evaluating the measurement model at the dimension level using repeated indicators of the latent variables. In the subsequent stage, the resulting latent variable score is used as the dimension score in the evaluation at the variable level.

RESULT

Measurement Model (Outer Model): First Order Construct

In the first-order construct, convergent validity was assessed through an evaluation of the outer loading and Average Variance Extracted (AVE) values.

Reliability testing of the first-order construct was conducted by examining the values of Cronbach's alpha and the composite reliability. Discriminant validity was determined by evaluating the Fornell-Larcker criterion values.

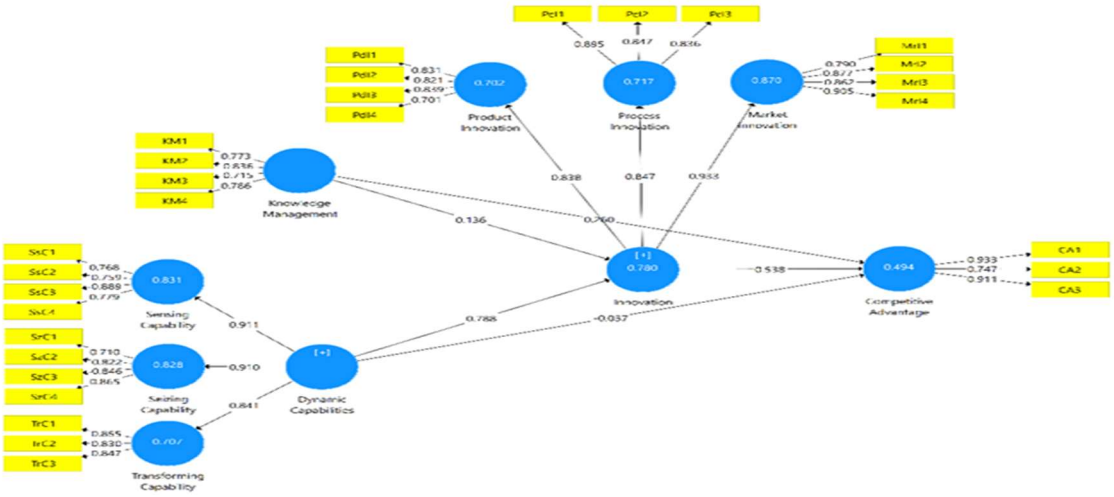

Figure 1. First-Order Construct

Convergent Validity and Reliability Test

Outer loading exhibits a significant level of validity when its value surpasses 0.70 (Hair et al., 2021). In other words, an indicator is considered valid and capable of measuring its construct or variable if the loading factor coefficient of the item is greater than 0.7. A variable or dimension is deemed valid if the Average Variance Extracted (AVE) value in the Convergent Validity test is over 0.50 (Hair et al., 2021). According to Hamid and Anwar (2019), the reliability test in Partial Least Squares (PLS) can be assessed through two methods: Cronbach's alpha and Composite reliability for each dimension tested in the first-order construct. A variable or dimension is considered reliable if the composite reliability (CR) and Cronbach's alpha values in the dimension reliability test are greater than 0.70.

Table 1. Construct Validity and Reliability Test Results (First-Order Construct)

Dimensions	First Order Construct				
	IND	**OL**	**AVE**	**CR**	**CA**
Product Innovation (PRI)	IPd1	0,831	0,640	0,928	0,914
	IPd2	0,821			
	IPd3	0,839			
	IPd4	0,701			
Market Innovation (MRI)	IPr1	0,790	0,739	0,923	0,908
	IPr2	0,877			
	IPr3	0,862			
	IPr4	0,905			
Process Innovation (PCI)	IPs1	0,895	0,739	0,919	0,881
	IPs2	0,847			
	IPs3	0,836			
Sensing Capability (SSC)	SsC1	0,768	0,641	0,895	0,823
	SsC2	0,759			
	SsC3	0,889			
	SsC4	0,779			
Seizing Capability (SZC)	SzC1	0,710	0,661	0,876	0,810
	SzC2	0,822			
	SzC3	0,846			
	SzC4	0,865			
Transforming Capability (TRC)	TrC1	0,855	0,712	0,900	0,832
	TrC2	0,830			
	TrC3	0,847			

Source: Processed Data (2024)

Based on Table 1, it can be seen that the results of the convergent validity evaluation through the testing of loading factors obtained **outer loading values are greater than 0.70 for all items or indicators. Thus, it can be said that the items used to measure each dimension of each variable are declared valid. The Average Variance Extracted (AVE) values were greater than 0.50 for all dimensions tested. Therefore, it can be stated that the dimensions used to measure each variable in the first-order construct are declared valid.

Table 1 also shows the results of the dimension reliability test through the testing of composite reliability and the Cronbach's alpha obtained. Composite reliability (CR) and Cronbach's alpha values were greater than 0.70 for all dimensions tested. Thus, it can be said that the dimensions used to measure each variable in the first-order construct are declared reliable.

Discriminant Validity: First-Order Construct

Table 2. Fornell-Larcker Criterion Test Results (First-Order Construct)

	Marketing innoation	Product innovation	Process innovation	Seizing capability	Sensing capability	Transforming capability
IPR	0,859					
IPD	0,674	0,800				
IPS	0,717	0,544	0,860			
SZC	0,668	0,614	0,716	0,813		
SSC	0,786	0,643	0,732	0,746	0,801	
TRC	0,659	0,617	0,713	0,653	0,652	0,844

Source: Processed Data (2024)

The Fornell-Larcker measure is used to assess the relationship between the square root of the average variance extracted (AVE) value and the latent variable. The requirement was that the square root of each AVE construct must exceed its correlation value with the remaining constructs. According to the results of the Fornell-Larcker criterion test presented in Table 2, the square root values for each AVE construct exceed their correlation values with other constructs, which suggests that the criteria for discriminant validity are satisfied.

Measurement Model (Outer Model): Second-Order Construct

After evaluating the measurement model in the first-order construct, the next step in the embedded two-stage approach is to evaluate the second-order construct, which focuses on testing the study variables.

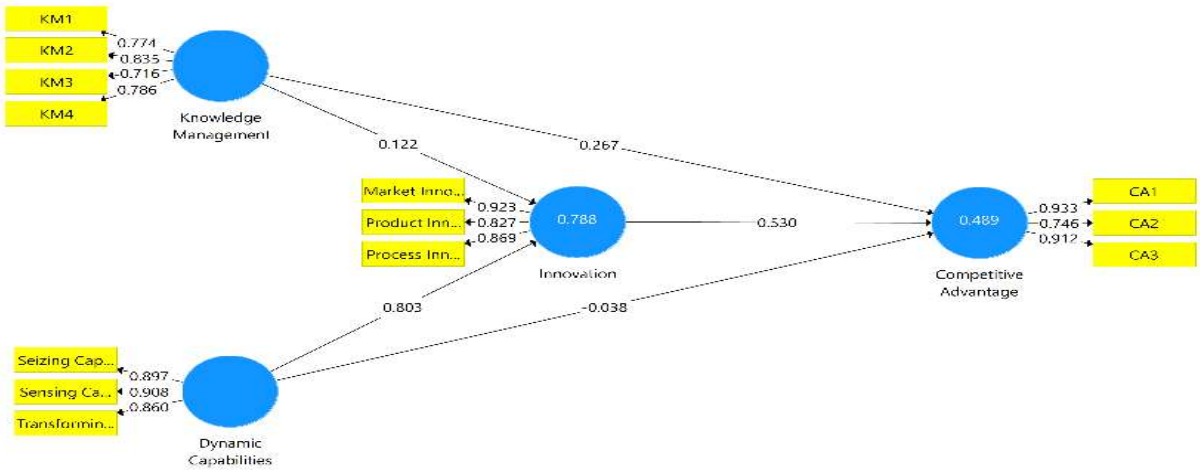

Figure 2. Second-Order Construct

At this stage, the latent variable scores of innovation and dynamic capabilities, which were previously the results of testing in the first-order construct, were used in the second stage as indicators to measure the variables connected to innovation and dynamic capabilities.

Table 3. Outer Loadings Factors

Construct	Second-order construct				
	IND	OL	AVE	CR	CA
Innovation	Market innovation	0,923	0,764	0,906	0,845
	Product innovation	0,827			
	Process innovation	0,869			
Competitive advantage	CA1	0,933	0,753	0,900	0,832
	CA2	0,746			
	CA3	0,912			
Knowledge management	KM1	0,933	0,607	0,860	0,784
	KM2	0,774			
	KM3	0,835			
	KM4	0,716			
Dynamic capabilities	Seizing capability	0,786	0,789	0,918	0,866
	Sensing capability	0,897			
	Transforming capability	0,908			
	Market innovation	0,860			

Source: Processed Data (2024)

As shown in Table 3, the results of convergent validity testing revealed that all items or indicators had outer loading values greater than 0.70. In addition, the convergent validity measurement showed Average Variance Extracted (AVE) values greater than 0.50 for all variables tested. These findings indicate that the dimensions used to measure each variable in the second-order construct were valid. Furthermore, the results of the variable reliability test through composite reliability testing showed that all variables tested had composite reliability (CR), and Cronbach's alpha values greater than 0.70, indicating that each variable in the second-order construct is reliable.

Discriminant Validity: Second-Order Construct

A discriminant validity test was conducted using the Fornell-Larcker criterion. Fornell-Larcker is a measure that compares the square root of the AVE value to the latent variable. The square root value of each AVE construct must be greater than its correlation value with other constructs.

Table 4. Fornell-Larcker Criterion Test Results (Second-Order Construct)

	Dynamic capabilities	Innovation	Competitive advantage	Knowledge management
Dynamic capabilities	0,888			
Innovation	0,883	0,874		
Competitive advantage	0,606	0,670	0,868	
Knowledge management	0,656	0,649	0,586	0,779

Source: Processed Data (2024)

According to the findings of the Fornell-Larcker criterion test in Table 4, it can be concluded that the square root value for each AVE construct is higher than its correlation value with other constructs. This suggests that the conditions for discriminant validity are fulfilled and present.

Structural Model Evaluation (Inner Model)

Coefficient of Determination (R-Square) Test for Dependent Construct

The magnitude of the coefficient of determination (R-squared) was used to measure the influence of other variables on the dependent variable. An R-square test result of 0.67 and above for the dependent latent variable in the structural model indicates that the influence of the independent variable on the dependent variable is included in the strong category. If the result was 0.33-0.67, it was included in the moderate category, and if the result was 0.19-0.33, it was included in the weak category.

Table 5. Determination Coefficients Results Test

	R Square	R Square Adjusted	Remarks
Innovation	0,788	0,783	Strong
Competitive advantage	0,489	0,473	Moderate

Source: Processed Data (2024)

Based on Table 5, the R-squared value for the innovation variable is 0.788. This indicates that the influence exerted by knowledge management and dynamic capabilities on innovation is strong. Furthermore, the R-squared value for competitive advantage was 0.489. This finding suggests that the impact of knowledge management and dynamic capabilities on competitive advantage is moderate.

DISCUSSION

This study examined the direct and indirect effects of the presence of independent, dependent, and mediating variables (intervening). For hypothesis testing using statistical values, the t-statistic value used for an alpha of 5% was 1.64 (Abdillah and Jogiyanto, 2013; Lengkey et al., 2020).

Table 6. Path Coefficients Direct Effect

	Original Sample (O)	M	STDEV	O/STDEV	P Values
DC → INOV	0,803	0,799	0,059	13,582	0,000
DC → KB	-0,038	-0,037	0,187	0,201	0,420
INOV → KB	0,530	0,533	0,202	2,622	0,004
KM → INOV	0,122	0,127	0,069	1,774	0,038
KM → KB	0,267	0,267	0,108	2,462	0,007

Source: Processed Data (2024)

The Influence of Innovation on Competitive Advantage

The innovation construct's influence on competitive advantage has a positive original sample (O) value of 0.530. The t-statistic value of 2.622 was greater than 1.64, and the p-value of 0.004 was smaller than 0.05. Thus, we accepted the first hypothesis (H1) that innovation has a positive and significant influence on competitive advantage in sago-processed MSMEs in the Meranti Islands Regency. This indicates that the better or higher the level of innovation carried out by sago-processed MSME actors in the Meranti Islands Regency, the more these MSMEs will be able to achieve a competitive advantage.

In line with these research results, a study conducted by Hatani (2022) stated that innovation has a positive influence on competitive advantage. On the other hand, research conducted by Sutrisno (2023) obtained results that are not in line with the findings of this study. The study finds that innovation has a negative effect on competitive advantage.

The Influence of Knowledge Management on Competitive Advantage

The knowledge management construct for competitive advantage has a positive original sample (O) value of 0.267. The t-statistic value of 2.462 was greater than 1.64, and the p-value of 0.007 was smaller than 0.05. Thus, we accepted the second hypothesis (H2) that knowledge management has a positive and significant influence on competitive advantage in sago-processed MSMEs in the Meranti Islands Regency. This shows that the better sago-processed MSME actors in the Meranti Islands Regency manage their knowledge, the more these MSMEs will be able to achieve competitive advantage.

The positive and significant influence of knowledge management on competitive advantage is in accordance with the results of research conducted by Kusuma and Efendi (2022), who stated that knowledge management has a positive and significant effect on competitive advantage. In contrast to the findings of this study, research conducted by Patrisia et al. (2022) found that knowledge management has a negative effect on competitive advantage.

The Influence of Knowledge Management on Innovation

The knowledge management construct for innovation had a positive original sample (O) value of 0.122. The t-statistic value of 1.774 was greater than 1.64, and the p-value of 0.038 was smaller than 0.05. Thus, we accepted the third hypothesis (H3), which states that knowledge management has a positive and significant influence on innovation in sago-processed MSMEs in the Meranti Islands Regency.

This shows that the better the sago-processed MSME actors in the Meranti Islands Regency are at managing their knowledge, the more these MSMEs will be able to create innovations in their business, including product innovation, process innovation, and market innovation.

The positive and significant influence exerted by knowledge management on innovation is in accordance with the results of research conducted by Ginting et al. (2023), who stated that knowledge management has a positive and significant effect on innovation. In contrast to the findings of this study, research conducted by Arief and Nursyamsiah (2022) found that knowledge management has a negative effect on innovation.

The Influence of Dynamic Capabilities on Competitive Advantage

The dynamic capabilities construct on competitive advantage has a negative original sample (O) value of -0.038. The t-statistic value of 0.201 was smaller than 1.64, and the p-value of 0.420 was greater than 0.05. Thus, we accepted the fourth hypothesis (H4) that dynamic capabilities have a positive and significant influence on competitive advantage in sago-processed MSMEs in the Meranti Islands Regency.

The lack of influence of the dynamic capabilities variable on the competitive advantage variable in this study is in line with the results of research conducted by Afif et al. (2019), who state that dynamic capabilities do not have a positive and significant effect on competitive advantage. This means that having dynamic capabilities does not guarantee that sago-processed MSMEs in the Meranti Islands Regency can achieve a competitive advantage. On the other hand, research conducted by Michael and Widjojo (2021) found that dynamic capabilities have a positive and significant effect on competitive advantage.

The Influence of Dynamic Capabilities on Innovation

The dynamic capabilities construct for innovation has a positive original sample (O) value of 0.803. The t-statistic value of 13.582 was greater than 1.64, and the p-value of 0.000 was less than 0.05. Thus, the fifth hypothesis (H5), which states that dynamic capabilities have a positive and significant influence on innovation in sago-processed MSMEs in the Meranti Islands Regency, is accepted. This shows that the higher or better the dynamic capabilities possessed by sago-processed MSME actors in the Meranti Islands Regency, the more they will enhance the ability of MSMEs to innovate, especially in product innovation, process innovation, and market innovation.

The positive and significant influence exerted by dynamic capabilities on innovation in sago-processed MSMEs in the Meranti Islands Regency is in line with the results of research conducted by Maulidina et al. (2023), who stated that dynamic capabilities have a positive and significant effect on innovation. Innovation is the result of dynamic capabilities that help organizations remain competitive and relevant in an ever-changing business environment.

Table 7. Path Coefficients Indirect Effect

	Original Sample (O)	M	STDEV	O/STDEV	P Values
DC → INOV→ KB	0,803	0,799	0,059	13,582	0,000
KM → INOV → KB	-0,038	-0,037	0,187	0,201	0,420

Source: Processed Data (2024)

The Influence of Knowledge Management on Competitive Advantage Through Innovation

The knowledge management construct of competitive advantage through innovation has a negative original sample (O) value of -0.038. The t-statistic value of 0.201 was smaller than 1.96, and the p-value of 0.420 was greater than 0.05. Thus, the sixth hypothesis (H6), which states that knowledge management has a positive and significant influence on competitive advantage through innovation in sago-processed MSMEs in the Meranti Islands Regency, is rejected. From these findings, it can be concluded that knowledge management does not have a positive and significant effect on competitive advantage through innovation.

The negative influence of knowledge management on competitive advantage through innovation is in line with research conducted by Lidaningrum (2023), who found that product innovation is not able to mediate the influence of knowledge management and competitive advantage. This shows that a better level of knowledge management through created innovation does not guarantee that competitive advantage will be achieved. In contrast to the findings of this study, research conducted by Samsir et al. (2017) found that innovation mediates the relationship between knowledge management and competitive advantage. This relationship indicates that the higher the knowledge management carried out by MSMEs, the higher the level of achievement of competitive advantage if done through innovation.

The Influence of Dynamic Capabilities on Competitive Advantage Through Innovation

The dynamic capabilities construct of competitive advantage through innovation has a positive original sample (O) value of 0.803. The t-statistic value of 13.582 was greater than 1.64, and the p-value of 0.000 was less than 0.05. Thus, the seventh hypothesis (H7), which states that dynamic capabilities have a positive and significant influence on competitive advantage through innovation in sago-processed MSMEs in the Meranti Islands Regency, is accepted. From these findings, we can conclude that dynamic capabilities have a positive and significant effect on competitive advantage through innovation.

The positive and significant influence exerted by dynamic capabilities on competitive advantage through innovation in sago-processed MSMEs in the Meranti Islands Regency is in line with the results of research conducted by Ferreira et al. (2018), who stated that there is a direct and indirect influence between dynamic capabilities on competitive advantage as an effect of the innovation variable. This means that innovation is needed in MSMEs to face changes in the business environment to achieve a competitive advantage in the industry.

CONCLUSION AND RECOMMENDATION

Based on the research results described above, several conclusions can be drawn.

1. Innovation has a positive and significant influence on competitive advantage in sago-processed MSMEs in the Meranti Islands Regency.
2. Knowledge management has a positive and significant influence on competitive advantage in sago-processed MSMEs in the Meranti Islands Regency.
3. Knowledge management has a positive and significant influence on innovation in sago-processed MSMEs in the Meranti Islands Regency.
4. Dynamic capabilities have a negative and insignificant effect on competitive advantage in sago-processed MSMEs in the Meranti Islands Regency.
5. Dynamic capabilities have a positive and significant influence on innovation in sago-processed MSMEs in the Meranti Islands Regency.
6. Innovation does not mediate the influence of knowledge management and competitive advantage in sago-processed MSMEs in the Meranti Islands Regency.
7. Innovation mediates the influence between dynamic capabilities and innovation in sago-processed MSMEs in the Meranti Islands Regency.

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